

Documentary Credit

WORLD

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■ CORONAVIRUS AND LC PRACTICE

As the world comes to grips with the staggering health and economic impacts of the coronavirus, the letter of credit industry faces serious questions regarding key operational issues such as LC signatures and documentary presentation. Over a one-week period (13-20 March), DCW conducted a survey of LC specialists on the use of digital signatures and their approaches toward other LC procedural matters due to COVID-19. The collected and synthesized survey results are presented here. Reactions to the survey findings are then offered by experienced professionals Buddy Baker, Hugo Verschoren, Don Smith, and Carter Klein. Lawyers Michael Evan Avidon and Rachel Kwon follow up with insights on risk considerations relating to LCs and the coronavirus. Muhammad Sohail Hussain then challenges banks to evaluate their business continuity plans.

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GIVING CREDIT WHERE CREDIT IS DUE: LETTERS OF CREDIT AND THE NEW CORONAVIRUS*

by Michael Evan AVIDON and Rachel S. KWON**

Letters of credit (“LCs”) are irrevocable, independent and documentary payment mechanisms by which an issuing bank in effect substitutes its credit for that of an applicant. LCs play a key role in facilitating trade transactions and financial transactions by allowing parties to manage risk and alleviate uncertainty with respect to payment obligations. From an LC that is arranged by a Japanese cloth manufacturer in favor of a New York cloth seller,¹ to an LC that is arranged by a Benin



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company in favor of a Costa Rican company for the shipment of fish from Argentina to Benin,² LCs have resiliently demonstrated relevance to trade and financial transactions. In the rapidly changing economic and political environment we are facing due to the COVID-19 pandemic, parties to LCs are questioning how LCs and related documents (such as reimbursement agreements and sales agreements) allocate risks posed by the virus, and deciding how best to proceed moving forward.

Depending on the combination of several factors – the wording of a particular LC or contract, any applicable practice rules (such as UCP 600, ISP98, or URDG 758),³ or any applicable law (such as

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1. *Alaska Textile Co. v. Chase Manhattan Bank, N.A.*, 982 F.2d 813 (2d Cir. 1992).

2. *Vanpoy Corp. S.R.L. v. Soleil Chartered Bank*, 2019 N.Y. Slip Op. 30556 (Sup. Ct. Feb. 21, 2019).

3. These rules are more fully described as the Uniform Customs and Practice for Documentary Credits, 2007 revision, International Chamber of Commerce (“ICC”) Pub. No. 600; the International Standby Practices 1998, ICC Pub. No. 590; and the Uniform Rules for Demand Guarantees, effective July 1, 2009, ICC Pub. No. 758. Although URDG provides for the issuance of “guarantees” and “counter-guarantees,” these undertakings can qualify as letters of credit under UCC Article 5 and for convenience are also referred to herein as “LCs.”

Uniform Commercial Code⁴ (“UCC”) Article 5 and common law) – several issues may arise relating to how the issuing bank, beneficiary and applicant are each protected and obligated with respect to an LC given the global impact of COVID-19. A few of those issues are discussed below.

Consider first a beneficiary that wants to timely present its drawing documents to the issuing bank in order to obtain payment under an LC. Can an issuing bank that has closed its offices to prevent the spread of COVID-19 refuse to honor such drawing if the presentation is delayed until the bank reopens after the stated expiration date of the LC? The outcome may vary greatly depending on the wording of the LC, the applicable rules, the circumstances of the closure, and any attempted presentation. For example, UCP 600 focuses on whether force majeure (which, though not specifically defined, is referred to as causes of interruption including “any other causes beyond its control”) caused the closing and imposes the risk of a force majeure closing on the beneficiary. See UCP 600 Article 36. URDG 758 also focuses on force majeure, but provides for a 30-day extension from the date the LC would otherwise have expired (even if the force majeure lasts longer). See URDG 758 Article 26. ISP98 is not dependent on finding force majeure but refers simply to a closure on a business day, and provides for a 30-day extension from the reopening, if the bank reopens. See ISP98 Rule 3.14(a).

The beneficiary may ask how to satisfy the presentation requirements of the LC if the issuing bank’s offices are closed. Most LCs require paper presentation, unless the LC specifies otherwise or the LC is a standby LC, governed by ISP98 rules, issued to a bank and calling for presentation of only a demand for payment (in which latter case, the beneficiary is permitted to make a presentation through SWIFT (see ISP98 Rule 3.06(b))). While certain ISP98 rules give the issuing bank the option to accept a non-paper demand from the true beneficiary, that option is meaningful only if the demand is the only required drawing document (since any other documents specified to accompany the demand are still required to be presented). Of course if the parties are willing and able, the LC can be amended with everyone’s consent to provide for alternative means of presentation.

Prospective issuing banks and applicants may inquire whether new LCs can be issued or outstanding LCs can be amended if physical operations are hindered by office closures. As an example, between LCs being issued as electronic documents or via wet ink signatures on paper, what is permissible may depend on the applicable law and what is acceptable may depend on custom and practice. UCC Sec. 5-104 requires a “record” (a broadly defined term) and authentication by (1) signature (see UCC Sec. 1-201(b)(37) and (43) for definitions of “signed” and “writing”), or (2) (i) an “agreement of the parties” (which, for example, could be evidenced by exchanges of emails) or (ii) standard practice as referred to in UCC Sec. 5-108(e) (e.g., SWIFT)).

Where it may not be feasible or acceptable for the issuing bank to issue its LC directly to the beneficiary, an alternative may be to issue the LC via SWIFT to a bank that is requested to advise the LC to the beneficiary (who usually has an existing relationship with the advising bank).

There are a host of other LC-related issues posed by COVID-19. Parties may be able to manage risk by reviewing their rights and obligations under existing LCs and taking proactive steps.

For more information on how COVID-19 may impact your rights and obligations under an existing LC, or for any other information related to LCs, contact the authors or another Moses & Singer attorney. ■

4. All citations to the UCC in this article are to the New York Uniform Commercial Code.